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Choice of Forum in Tax Litigation

Arnold W. Reitze, Jr.

THREE COURTS of original jurisdiction are available to the potential tax litigant: the United States Tax Court,¹ the United States Court of Claims,² and the United States District Court.³ As will be demonstrated, the choice of forum dictates the procedural

options that may be followed and thus also influences, perhaps crucially, the ultimate outcome of the case.

The purpose of this article is to outline, as briefly as possible, the factors that should be considered in the choice of a forum.

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IS PAYMENT OF THE TAX NECESSARY?

A. Tax Court

The Tax Court⁴ may be used by the taxpayer without his having to pay the alleged tax deficiency,⁵ except in the following instances:

1. Where the taxpayer has waived his rights on assessment and collection (Form 870).⁶
2. Where the Secretary or his delegate believes that the assessment or collection of a deficiency will be jeopardized by delay.⁷

¹ INT. REV. CODE OF 1954, § 7442 [hereinafter cited as CODE].

² 28 U.S.C. § 1491 (1964).

³ *Id.* §§ 1346, 1402 (1964).

⁴ Prior to 1942, this court was known as the United States Board of Tax Appeals. Technically, the Tax Court is an independent agency in the executive branch of the Government. *Lasky v. Commissioner*, 352 U.S. 1027 (1957). For a brief discussion of the Tax Court, see Babbitt & Morris, *An Introduction to the Tax Court of the United States*, 21 TAX LAWYER 615 (1968).

⁵ CODE § 6213(a). This statutory restriction on collection of the tax is important since section 7421 places nearly absolute prohibitions on the use of equitable doctrines to prevent the assessment or collection of taxes. For the background of the allowance of suits prior to the paying of taxes, see H. BICKFORD, *SUCCESSFUL TAX PRACTICE* 262 (4th ed. 1967). See also Lore, *Common Mistakes in Trying Tax Court Cases*, 11 TAX COUNSELOR'S Q. 19 (1967).

⁶ CODE § 6213(d).

⁷ *Id.* § 6861.

3. Where a taxpayer is involved in bankruptcy or receivership proceedings.⁸

Mathematical errors, corrected by the Internal Revenue Service, neither constitute a deficiency notice nor allow for an appeal to the Tax Court.⁹ Excess overassessments under section 6411 attributable to carryback adjustments can be treated as if they were mathematical errors.¹⁰

If the Tax Court decides against the taxpayer, when the decision becomes final the additional tax due will be increased by 6 percent per annum interest from the due date of the return.¹¹ If there is a reasonable chance the taxpayer will lose, he may be wise to pay the deficiency. If this is done after the deficiency notice (90-day letter) is received, the Tax Court will still have jurisdiction.¹² Then, if the taxpayer prevails, he will receive his overpayment back and the Government will pay him 6 percent interest.¹³

B. *Court of Claims and the District Court*

Payment in full of the assessed tax is a jurisdictional prerequisite to suit in the Court of Claims or the District Court.¹⁴ However, concurrent jurisdictional problems can occasionally arise.¹⁵ Normally, once an election of forum is made, it is irrevocable.

JURISDICTIONAL PREREQUISITES

A. *Tax Court*

1. The Secretary of the Treasury must determine that a deficiency exists.¹⁶

2. A deficiency notice must be sent to the taxpayer by certified or registered mail.¹⁷

⁸ *Id.* § 6871.

⁹ *Id.* § 6213(b)(1).

¹⁰ *Id.* § 6213(b)(2).

¹¹ *Id.* § 6601.

¹² *Id.* § 6213(b)(3).

¹³ *Id.* § 6611(a).

¹⁴ *Flora v. United States*, 357 U.S. 63 (1958), *aff'd on rehearing*, 362 U.S. 145 (1960).

¹⁵ If the taxpayer files a refund claim and then 6 months later files a *District Court* suit, there can be problems if a notice of deficiency is sent about the same time. The problem arises because section 6213 stays an assessment only if a petition is filed with the *Tax Court*. H. BICKFORD, *supra* note 5, at 265. See also 152 TAX MANAGEMENT PORTFOLIO, *Tax Court Litigation (Pt. 1)*, at A-19.

¹⁶ CODE § 6212(a).

¹⁷ *Id.*

3. Within 90 days after the notice of deficiency is mailed (150 days if addressed to a person outside the United States), the taxpayer must file a petition with the Tax Court.¹⁸

If all of these requirements are not met, notwithstanding section 7421(a), further proceedings may be enjoined.¹⁹

B. Court of Claims and the District Court

1. A full payment of the tax must be made.²⁰

2. A timely filing of a claim of refund with the Internal Revenue Service is necessary.²¹ This claim is very important for it is, in effect, the complaint in later litigation.²²

3. No suit may be commenced before the expiration of 6 months from the date of the filing of the claim unless the Secretary or his delegate denies the claim for refund before the 6-month period elapses.²³

4. No suit may be begun after 2 years from the date of mailing of the notice of disallowance from the Secretary or his delegate.²⁴

SUBJECT OF JURISDICTION

A. Tax Court

The Tax Court's jurisdiction is limited to income, estate, gift, and excess profits taxes. It does not have jurisdiction over excise, stamp, or alcohol taxes.²⁵

B. Court of Claims and the District Court

The Court of Claims and the District Court have jurisdiction in cases involving any type of federal tax.

¹⁸ *Id.* § 6213(a).

¹⁹ *Id.*

²⁰ *Flora v. United States*, 357 U.S. 63 (1958), *aff'd on rehearing*, 362 U.S. 145 (1960). See also *Kell-Strom Tool Co. v. United States*, 205 F. Supp. 190 (D. Conn. 1962) (payment of interest on tax not required).

²¹ CODE §§ 6532, 7422.

²² See McDowell, *Traps in Refund Claims and Filing Returns*, N.Y.U. 16TH INST. ON FED. TAX. 485 (1958); Pomeroy, *Refund Claims: Litigation*, N.Y.U. 21ST INST. ON FED. TAX. 129 (1963); Roberts, *Tips on a Refund Suit in the District Courts*, 37 TAXES 493 (1959).

²³ CODE § 6532(a).

²⁴ *Id.* See also *id.* § 7442.

²⁵ *Id.* § 7442.

PARTIES

A. *Tax Court*

The proper party is the person against whom the Commissioner determined the deficiency. The respondent is the Commissioner.²⁶

B. *Court of Claims and the District Court*

The proper plaintiff is the taxpayer or his successor. Since the refund suit against the District Director was abolished on February 1, 1967, the proper defendant in all tax cases is the United States.²⁷

PRECEDENT

At any given time the various courts deciding tax cases may have inconsistent positions on a given subject, with one or more of them demonstrating a favorable or unfavorable proclivity toward the taxpayer's position. Thus, the decisions of each tribunal must be reviewed.²⁸ This review would involve consideration of the decisions of the appropriate Circuit Court of Appeals for the Tax Court or District Court.²⁹ The Court of Claims is the court most likely not to consider itself bound by decisions of the Tax Court or Court of Appeals and in many instances has held Treasury regulations invalid.³⁰

STATISTICS ON TAXPAYER SUCCESS

Statistics show that the taxpayer has won more cases in the District Court than in the Tax Court,³¹ but that it may be easier to settle cases in the Tax Court. There seems, however, to be no significant difference between the District Court and the Court of Claims.³²

²⁶ TAX CT. R. PRAC. 6.

²⁷ CODE § 7422(f). See generally La Force, *The Federal District Court Tax Refund Suit: A Primer*, 20 ABA TAXATION SECTION 129, 131 (1967).

²⁸ See Pavenstedt, *The United States Court of Claims as a Forum for Tax Cases*, 15 TAX L. REV. 1 (1959). Pavenstedt reviews areas in which the Court of Claims is more favorable to the taxpayer than other courts. *Id.* at 8 n.27. He also explores areas in which the Court of Claims is less favorable to the taxpayer. *Id.* at 10 n.28.

²⁹ For a further discussion of this subject, see L. KEIR, *TAX COURT PRACTICE* 21 (1960); Gannet, *Pre-Trial Strategy in a Tax Case: Choice of Forum: a Checklist of Points to Consider*, N.Y.U. 22D INST. ON FED. TAX. 75, 88 (1964); 152 TAX MANAGEMENT PORTFOLIO, *supra* note 15, at A-20.

³⁰ Pavenstedt, *supra* note 28, at 217.

³¹ H. BICKFORD, *supra* note 5, at 269.

³² Pavenstedt, *supra* note 28, at 10-11.

AMOUNTS IN CONTROVERSY

One writer reports the breakdown of average value per case as \$589,000 for the Court of Claims, \$110,000 for the District Court, and \$79,000 for the Tax Court.³³ A more recent survey, in 1966, indicates that the Court of Claims average was \$400,000 while the average of the District Courts may be less than \$70,000.³⁴ It seems clear, at least, that the Court of Claims is most conditioned to thinking in terms of large sums.

THE COURT AND ITS COMPOSITION

A. *Tax Court*

One of 16 judges who travel from Washington will hear the case. The tax background of the members, their terms of office, and central control from Washington give the Tax Court more expertise and uniformity than the other courts.³⁵ The Tax Court, however, may place the most pressure on the taxpayer for a quick trial as the court may handle 100 cases in 2 weeks when visiting a given city.³⁶

B. *Court of Claims*

The Court of Claims sits in Washington, D.C. in two panels of three judges. This court, much like the Tax Court, possesses expertise in tax matters. It has the advantage of having little compunction against deciding that large sums should be paid by the United States.³⁷

C. *District Court*

District Court judges may be more familiar with local problems, for example, coal mining casualty losses in Pennsylvania. They may also be more willing to exclude evidence on technical grounds.

PUBLICITY

Publicity, which is probably undesired by the taxpayer, is

³³ *Id.* at 11.

³⁴ Kipps, *A Unique National Court: The United States Court of Claims*, 53 A.B.A.J. 1025, 1026 (1967), quoting Miller, *Tax Litigation in the Court of Claims*, 55 GEO. L.J. 454 (1966).

³⁵ L. KERR, *supra* note 29, at 8-17.

³⁶ Durkan, *Your First Tax Case*, 47 A.B.A.J. 173, 175 (1961).

³⁷ Kipps, *supra* note 34, at 1026.

roughly related to the distance between the place of the trial and the taxpayer's home.

A. Tax Court

The Tax Court sits in many cities. The taxpayer may request the place where he would prefer the trial to be held.³⁸ The court then fixes the place of trial, in its discretion, so as to cause "as little inconvenience and expense to taxpayers as is practicable."³⁹

B. Court of Claims

The Court of Claims, as mentioned above, sits in Washington, D.C.⁴⁰

C. District Court

The District Court will in all probability result in the greatest publicity both because of geographical proximity to the taxpayer's home⁴¹ and because of newspaper coverage practices.⁴²

JURY TRIAL

A jury trial is available only in the District Court and it may be demanded by either the taxpayer or the Government.⁴³ Jury trials may be useful in determining questions of fact.⁴⁴ They result in about 60 percent taxpayer success, according to one study, with a substantial portion of the jury trials taking place in the Southern States.⁴⁵

BURDEN OF PROOF

The burden of proof requirements vary, but, this seems to lead

³⁸ TAX CT. R. PRAC. 26(a). Cities in which the Tax Court sits are found in the *Rules of Practice*, Appendix II.

³⁹ CODE § 7446.

⁴⁰ Kipps, *supra* note 34, at 1025.

⁴¹ The place of District Court actions is controlled by 28 U.S.C. §§ 1391(a), 1402(a) (1964).

⁴² 152 TAX MANAGEMENT PORTFOLIO, *supra* note 15, at A-23.

⁴³ 28 U.S.C. § 2402 (1964). Demand for a jury trial must be made within the time specified by FED. R. CIV. P. 38.

⁴⁴ See Holzman, *Should You Use a Jury?*, 36 TAXES 301 (1958). Mr. Holzman analyzes 75 tax cases utilizing juries according to the issues involved and the results.

⁴⁵ Walston, *The Use of Juries in Federal Civil Income Tax*, 39 TAXES 144, 147 (1961).

to no significant difference among forums.⁴⁶ However, some writers feel that difference in procedure is significant.⁴⁷

DANGER OF INCREASED TAX DEFICIENCY

A petition in the Tax Court may be answered by a demand for an increased deficiency.⁴⁸ The same thing can happen in the District Court, but, if the deficiency is paid after the statutory notice is issued and the taxpayer waits until the statute of limitations has run on the assessment of additional deficiencies before filing the refund suit,⁴⁹ then the worst that can happen is that the Commissioner may use his claim as a setoff against the refund.⁵⁰

PERSONS ADMITTED TO PRACTICE

Any lawyer may be admitted to practice before the three different courts.⁵¹ Nonlawyers may be admitted to practice before the Tax Court.⁵² None of the courts require specialists, but litigants in 47 percent of the cases argued before the Court of Claims between 1949 and 1958 used Washington counsel.⁵³

AVAILABILITY OF DISCOVERY

A. Tax Court

There is no discovery available in the Tax Court.

B. Court of Claims

Discovery is allowed in a manner similar to that in the District Court except that such discovery is at the discretion of the court.⁵⁴

⁴⁶ 152 TAX MANAGEMENT PORTFOLIO, *supra* note 15, at A-20.

⁴⁷ See Gannet, *supra* note 29, at 87; Whitfield & McCallum, *Burden of Proof and Choice of Forum in Tax Litigation*, 20 VAND. L. REV. 1179 (1967).

⁴⁸ Joseph B. Ferguson, 47 T.C. 11 (1966). An amended answer increased the deficiency from \$1,191.52 to \$310,000. The \$310,000 was successfully maintained by the Government. See also John J. Raskob, 37 B.T.A. 1283 (1938); Ash, *Factors in Selecting the Forum in Which To Litigate*, N.Y.U. 12TH INST. ON FED. TAX. 935, 940-41 (1954).

⁴⁹ L. KEIR, *supra* note 29, at 27-28.

⁵⁰ See Ash, *supra* note 48, at 941.

⁵¹ CT. CL. R. 75 covers admissions to practice. The Tax Court admission is obtained by filling out the application obtained from the Enrollment Clerk of the Tax Court.

⁵² TAX CT. R. PRAC. 2.

⁵³ Pavenstedt, *supra* note 28, at 12.

⁵⁴ CT. CL. R. 30-41 (discovery and depositions). Arguments are made for and

C. District Court

Discovery is a matter of right in the District Court.⁵⁵ However, the Government can also use this technique against the taxpayer as it affirmatively investigates him.⁵⁶ In addition, the Government may object to discovery on the ground of "executive privilege."⁵⁷

SUBPOENAS

A. Tax Court

The Tax Court may issue subpoenas that may be served anywhere in the United States,⁵⁸ but they can only be enforced by the District Court.⁵⁹

B. Court of Claims

The Court of Claims may authorize and enforce the service of a subpoena anywhere in the United States⁶⁰ since it is an article III court.⁶¹

C. District Court

The District Court may order a subpoena to be served within the district or anywhere outside the district but still within 100 miles of the place of trial.⁶²

SETTLEMENT PROCEDURES

A. Tax Court

Settlement is subject to the concurrent jurisdiction of the Appellate Division of the Internal Revenue Service and the Regional

against allowing discovery in the Tax Court in Ritholz, *Diverse Views on Discovery in the Tax Court*, 21 TAX LAWYER 639 (1968).

⁵⁵ FED. R. CIV. P. 26.

⁵⁶ La Force, *supra* note 27, at 134.

⁵⁷ Taubeneck & Sexton, *Executive Privilege and the Court's Right To Know — Discovery Against the United States in Civil Actions in Federal District Courts*, 48 GEO. L.J. 486 (1960).

⁵⁸ CODE § 7456(a)(1).

⁵⁹ *Id.* § 7402(b).

⁶⁰ CT. CL. R. 51.

⁶¹ 28 U.S.C. § 171 (1958).

⁶² FED. R. CIV. P. 45.

Counsel until the opening date of a Tax Court trial session at which time the Regional Counsel receives full responsibility.⁶³

B. Court of Claims and the District Court

A suit in these courts is subject to the jurisdiction of the Tax Division of the Department of Justice. Forty-five Washington-based trial lawyers handle 90 percent of the tax refund cases.⁶⁴ All tax litigation routes result in a substantial percentage of settlements. Which route to choose depends upon local personalities and the attitudes of the Internal Revenue Service concerning the particular problem.

COSTS

A. Tax Court

Filing fees in the Tax Court are \$10.⁶⁵ An unusual economy provision is that briefs may be typed.⁶⁶ In general, this is thought to be the most inexpensive court.⁶⁷

B. Court of Claims

The major expense in the Court of Claims is the necessary travel to Washington and perhaps the use of outside counsel.

C. District Court

This court can offer an advantage in savings since it is a local court. However, higher overall costs may arise because of the court's formal procedure, particularly discovery.

LENGTH OF TIME OF LITIGATION

A. Tax Court

Tax Court litigation involves a minimum of 2 years' litigation time.⁶⁸

⁶³ L. KEIR, *supra* note 29, at 90.

⁶⁴ La Force, *supra* note 27, at 133. Tax cases in the Southern District of New York, and the Southern and Northern Districts of California are covered from tax sections created in the offices of the respective United States Attorneys. A field office, also staffed by Tax Division personnel, covers five Southwestern States from Fort Worth, Texas.

⁶⁵ CODE § 7451.

⁶⁶ TAX. CT. R. PRAC. 4.

⁶⁷ 152 TAX MANAGEMENT PORTFOLIO, *supra* note 15, at A-23.

⁶⁸ *Id.* at A-24.

B. *Court of Claims*

The Court of Claims' docket is current and its flexible schedule allows for a fairly prompt hearing. Decisions are announced from 1 to 3 months after oral argument.⁶⁹

C. *District Court*

Times vary, but due to the number of docketed cases the wait may be substantial.⁷⁰

REMEDIES

Equitable remedies, such as equitable recoupment for offsetting taxes barred by the statute of limitations, are not available in the Tax Court.⁷¹

TRIAL

A. *Tax Court*

The Tax Court's trial procedure is the least formal of the three different courts.

B. *Court of Claims*

The Court of Claims' trial procedure is the least technical of the courts and it is the most willing to apply equitable principles.

C. *District Court*

The District Court is the most formal of the courts; however, restrictive evidentiary rules can favor the taxpayer.

RIGHT OF APPEAL

A. *Tax Court*

Appeals may be taken to the United States Court of Appeals and then to the Supreme Court upon certiorari.⁷² Cases are reviewed in the same manner as in a District Court trial without a jury.⁷³

⁶⁹ Kipps, *supra* note 34, at 1029.

⁷⁰ Gannet, *supra* note 29, at 91.

⁷¹ Pavenstedt, *supra* note 28, at 207-08.

⁷² CODE § 7482.

⁷³ *Id.*

B. *Court of Claims*

Appeals may be taken only to the Supreme Court on writ of certiorari.⁷⁴ Therefore, the Court of Claims represents, in actuality, the only opportunity to succeed in court. Between 1949 and 1958, the Government filed only 11 petitions for certiorari; nine were granted. Few taxpayers are ever granted writs.⁷⁵ If a writ is granted, the review is limited to questions of law.⁷⁶

C. *District Court*

Appeals may be taken to the United States Court of Appeals,⁷⁷ and then to the Supreme Court upon certiorari.⁷⁸ When the trial is without a jury, review is similar to that given to decisions of the Tax Court. A jury verdict will be upheld unless there is no substantial evidence in the record to uphold it.⁷⁹

CONCLUSION

No single consideration of those previously discussed can be considered the most important. All of these factors presented, plus the infinite variables evolving from the personalities engaged in the litigation, become relevant. This is why trial practice is an art and not a science. The attorney must weigh as many of the variables as he can comprehend that relate to the problems of his specific case. The judgment and, thus, the decision is his. No formula will replace it.

⁷⁴ U.S. SUP. CT. R. 19.

⁷⁵ Pavenstedt, *supra* note 28, at 20-21.

⁷⁶ U.S. SUP. CT. R. 19.

⁷⁷ FED. R. CIV. P. 73.

⁷⁸ U.S. SUP. CT. R. 19.

⁷⁹ *Norwitt v. United States*, 195 F.2d 127 (9th Cir.), *cert. denied*, 344 U.S. 817 (1952).